
PROLYSIS LIMITED

OFFICERS AND ADMINISTRATION

DIRECTORS

Dr S Ruston
Professor J Errington
J S Garner
L T Clay

SECRETARY

Aldwych Secretaries Limited

AUDITORS

Richardsons
Chartered Accountants
30 Upper High Street
Thame
Oxfordshire
OX9 3EZ

SOLICITORS

Manches
9400 Garsington Road
Oxford Business Park
Oxford
OX4 2HN

REGISTERED OFFICE

6, Begbroke Business and Science Park
Sandy Lane
Yarnton
Oxford
OX5 1PF

COMPANY NUMBER

3548262



PROLYSIS LIMITED

DIRECTORS' REPORT

The directors present their report and financial statements for the year ended 31 December 2006.

PRINCIPAL ACTIVITY

The principal activity of the company during the year continued to be that of antimicrobial research.

DIRECTORS AND THEIR INTERESTS

The directors holding office during the period and their interests in the share capital of the company were as follows:

	At 31 December 2006 0.01p Ordinary shares	At 31 December 2005 0.01p Ordinary shares
J S Garner	-	-
L T Clay	-	-
S Ruston	-	-
<i>Share options (granted, not exercised)</i>	1,338,633	1,005,300
J Errington	3,260,000	3,260,000
<i>Share options (granted, not exercised)</i>	650,000	650,000
A D Guise		
(appointed 14/02/06 and resigned 25/09/06)	-	-

Messrs Clay's and Garner's personal interests in the company are held through East Hill University Spinouts III LLC. Messrs Clay and Garner are members of that LLC, the managing member of which is East Hill Advisors. East Hill University Spinouts III LLC is a company focussed on investment in early stage university spinout businesses.

The major shareholder is East Hill Management LLC who currently hold 76.1% of the issued share capital.

DIRECTORS' RESPONSIBILITIES

The directors are responsible for preparing this report and the financial statements in accordance with applicable law and United Kingdom Generally Accepted Accounting Practice. Company law requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the company at the year end and of the profit or loss of the company for that year. In preparing those financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent; and

PROLYSIS LIMITED

DIRECTORS' REPORT

DIRECTORS' RESPONSIBILITIES (CONTINUED)

- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the company and which enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities. The directors must also, in determining how amounts are presented within items in the profit and loss account and balance sheet, have regard to the substance of the reported transactions or arrangement, in accordance with generally accepted accounting principles or practice.

So far as the directors are aware, there is no relevant audit information of which the company's auditors are unaware. The directors have taken all the steps that they ought to have taken to make themselves and the company's auditors aware of any relevant audit information.

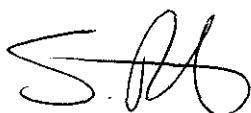
AUDITORS

In accordance with Section 385 of the Companies Act 1985, a resolution proposing that Richardsons be reappointed as auditors of the company will be put to the members at the Annual General Meeting.

SMALL COMPANY EXEMPTIONS

The above report has been prepared in accordance with the special provisions of Part VII of the Companies Act 1985 relating to small companies.

Signed on behalf of the Board of Directors



DR S RUSTON
DIRECTOR

Date: 26th Feb 2007.....

INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF

PROLYSIS LIMITED

We have audited the financial statements of Prolysis Limited for the year ended 31 December 2006 which comprise the profit and loss account, the balance sheet and the related notes 1 to 12. These financial statements have been prepared under the accounting policies set out therein, in accordance with the Financial Reporting Standard for Smaller Entities (effective January 2005) and the historical cost convention.

This report is made solely to the company's members, as a body, in accordance with section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

As described in the Directors' Report, the company's directors are responsible for the preparation of the financial statements in accordance with applicable law and United Kingdom Accounting Standards.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion the information given in the Directors' Report is consistent with the financial statements.

In addition we report to you if, in our opinion, the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read the Directors' Report and consider the implications for our report if we become aware of any apparent misstatements within it.

BASIS OF OPINION

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed.

INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF

PROLYSIS LIMITED

BASIS OF OPINION (CONTINUED)

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

OPINION

In our opinion the financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice applicable to smaller entities, of the state of the company's affairs as at 31 December 2006 and of its result for the year then ended and have been properly prepared in accordance with the Companies Act 1985. The information given in the Directors' Report is consistent with the financial statements.

Richardsons

RICHARDSONS
Chartered Accountants
Registered Auditors

30 Upper High Street
Thame
Oxfordshire
OX9 3EZ

26 February 2007

PROLYSIS LIMITED

PROFIT AND LOSS ACCOUNT FOR THE YEAR ENDED 31 DECEMBER 2006

NOTES	<u>2006</u>	<u>2005</u>
2(a) TURNOVER	-	-
Cost of sales	<u>-</u>	<u>-</u>
GROSS PROFIT		-
Administrative expenses	(2,676,782)	(3,308,040)
Other operating income	<u>-</u>	<u>90,000</u>
3 OPERATING LOSS	(2,676,782)	(3,218,040)
Interest receivable	33,801	57,040
Interest paid to investors	<u>-</u>	<u>(120,372)</u>
LOSS ON ORDINARY ACTIVITIES BEFORE TAXATION	(2,642,981)	(3,281,372)
4 Taxation	<u>290,346</u>	<u>267,391</u>
LOSS ON ORDINARY ACTIVITIES AFTER TAXATION	(2,352,635)	(3,013,981)
Retained loss brought forward	<u>(10,888,045)</u>	<u>(7,874,064)</u>
RETAINED LOSS CARRIED FORWARD	<u>£(13,240,680)</u>	<u>£(10,888,045)</u>

PROLYSIS LIMITED**BALANCE SHEET AS AT 31 DECEMBER 2006**

NOTES		<u>2006</u>	<u>2005</u>
	FIXED ASSETS		
5	Tangible assets	<u>80,840</u>	<u>107,298</u>
		80,840	107,298
	CURRENT ASSETS		
6	Debtors	382,917	407,697
	Cash at bank and in hand	<u>1,180,049</u>	<u>1,592,282</u>
		1,562,966	1,999,979
7	CREDITORS: amounts falling due within one year	<u>(2,289,880)</u>	<u>(1,891,994)</u>
	NET CURRENT (LIABILITIES)/ASSETS	<u>(726,914)</u>	<u>107,985</u>
	TOTAL ASSETS LESS CURRENT LIABILITIES	<u>(646,074)</u>	<u>215,283</u>
	NET (LIABILITIES)/ASSETS	<u>£ (646,074)</u>	<u>£ 215,283</u>
	CAPITAL AND RESERVES		
8	Called up share capital	6,610	5,860
9	Share premium account	11,587,835	10,097,307
9	Capital redemption reserve	1,000,161	1,000,161
9	Profit and loss account	<u>(13,240,680)</u>	<u>(10,888,045)</u>
	SHAREHOLDERS' FUNDS	<u>£ (646,074)</u>	<u>£ 215,283</u>

The financial statements have been prepared in accordance with the special provisions relating to small companies within Part VII of the Companies Act 1985 and the Financial Reporting Standard for Smaller Entities (effective January 2005).

The financial statements were approved by the Board of Directors and authorised for issue as dated below

.....Dr S Ruston – Director.....26th Feb 2007.....Date

PROLYSIS LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2006

1. GOING CONCERN

Cash flow forecasts in respect of the year ending 31 December 2006, show that the company's current financial resources are sufficient for the period to the end of March 2008. In order to continue in operational existence past this date, further funds will be required by the company.

The financial statements have been prepared on the going concern basis which assumes that the company will continue in operational existence for the foreseeable future. The validity of this assumption depends upon the success of the proposed share issue. The financial statements do not include any adjustments that would result if insufficient funds were available.

Despite the inherent uncertainty as to the outcome of the matter mentioned above, the directors are confident of a successful conclusion, and therefore believe that it is appropriate for the financial statements to be prepared on the going concern basis.

2. ACCOUNTING POLICIES

Accounting convention

The financial statements are prepared under the historical cost convention, and in accordance with the Financial Reporting Standard for Smaller Entities (effective January 2005) and the accounting policies adopted below.

(a) Turnover

Turnover represents amounts invoiced to third parties, net of VAT and trade discounts.

(b) Tangible fixed assets and depreciation

Fixed assets are recorded at cost, less depreciation.

Depreciation is provided, on a straight-line basis, at rates calculated to write off the cost, less estimated residual value, over the expected useful life of each asset as follows:

Bioinformatics system	3 years
Administration equipment and computers	2 years
Laboratory equipment	5 years
Leasehold improvements	5 years
Furniture	4 years

(c) Research and development

Expenditure on research and development is written off in the year in which it is incurred.

PROLYSIS LIMITED**NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED
31 DECEMBER 2006**

2. ACCOUNTING POLICIES (CONTINUED)**(d) Leasing and hire purchase commitments**

Assets held under finance leases and hire purchase contracts, which are those where substantially all the risks and rewards of ownership of the asset have passed to the company, are capitalised in the balance sheet and are depreciated over their useful lives. The corresponding lease or hire purchase obligation is treated in the balance sheet as a liability.

The interest element of the rental obligations is charged to the profit and loss account over the period of the lease and represents a constant proportion of the balance of capital repayments outstanding.

Rentals paid under operating leases are charged to income on a straight line basis over the lease term.

(e) Pensions

The company operates a group personal pension plan covering all employees. Contributions are charged to the profit and loss account as they become payable in accordance with the rules of the scheme. The assets of the scheme are held separately from those of the company in an independently administered fund.

(f) Government grants

Government grants of a revenue nature are related to research in applied genomics. They are credited to laboratory operating costs in the profit and loss account in the period in which they are incurred and discharged.

(g) Foreign currency transactions

Assets and liabilities denominated in foreign currencies are translated at the rate of exchange ruling at the balance sheet date. Transactions in foreign currencies are recorded at the rate ruling at the date of the transaction. All differences are taken to the profit and loss account.

(h) Deferred taxation

Deferred tax arises as a result of including items of income and expenditure in taxation computations in periods different from those in which they are included in the company's financial statements. Deferred tax is provided in full on timing differences which result in an obligation to pay more (or less) tax at a future date, at the average tax rates that are expected to apply when the timing differences reverse, based on current tax rates and laws. Deferred tax assets are recognised to the extent that it is regarded as more likely than not that they will be recovered. Deferred tax assets and liabilities are not discounted.

PROLYSIS LIMITED**NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED
31 DECEMBER 2006**

3. OPERATING LOSS

	<u>2006</u>	<u>2005</u>
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This is stated after charging/(crediting):

Auditors' remuneration	8,050	7,750
Directors' emoluments	192,583	186,245
Pension costs	46,036	44,770
Government grants received	-	(90,000)
Amortisation	-	20,834
Depreciation (owned assets)	55,086	57,054
Depreciation (leased assets)	<u>-</u>	<u>553</u>

One director (2005: one) is a member of the group personal pension plan.

4. TAX ON PROFITS ON ORDINARY ACTIVITIES

Corporation tax	<u>£ (290,346)</u>	<u>£ (267,391)</u>
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5. TANGIBLE FIXED ASSETS

	<u>Equipment</u>	<u>Leasehold Improvements</u>	<u>Furniture</u>	<u>Total</u>
COST:				
At 1 January 2006	1,238,929	215,393	13,612	1,467,934
Additions	13,000	15,628	-	28,628
Disposals	(151,438)	-	-	(151,438)
At 31 December 2006	<u>£1,100,491</u>	<u>£ 231,021</u>	<u>£ 13,612</u>	<u>£1,345,124</u>
DEPRECIATION:				
At 1 January 2006	1,141,335	209,211	10,090	1,360,636
Provided during the year	48,925	4,222	1,939	55,086
Disposals	(151,438)	-	-	(151,438)
At 31 December 2006	<u>£1,038,822</u>	<u>£ 213,433</u>	<u>£ 12,029</u>	<u>£1,264,284</u>
NET BOOK VALUE:				
At 31 December 2006	<u>£ 61,669</u>	<u>£ 17,588</u>	<u>£ 1,583</u>	<u>£ 80,840</u>
At 31 December 2005	<u>£ 97,594</u>	<u>£ 6,182</u>	<u>£ 3,522</u>	<u>£ 107,298</u>

The net book value of fixed assets above includes an amount of £nil (2005: £1,452) in respect of assets held under hire purchase contracts.

PROLYSIS LIMITED**NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED
31 DECEMBER 2006**

6. DEBTORS	<u>2006</u>	<u>2005</u>
Other debtors	355,524	356,839
Prepayments and accrued income	<u>27,393</u>	<u>50,858</u>
	<u>£ 382,917</u>	<u>£ 407,697</u>

The aggregate amount of debtors due after more than one year is £31,206 (2005: £31,206).

7. CREDITORS: amounts falling due within one year

Obligations under finance leases and hire purchase contracts	276	791
Trade creditors	228,236	257,966
Other taxes and social security costs	28,513	23,912
Other creditors	2,000,036	1,501,125
Accruals	<u>32,819</u>	<u>108,200</u>
	<u>£2,289,880</u>	<u>£1,891,994</u>

Included in "Other creditors" is £36 (2005: £31), relating to amounts due to the defined contribution pension scheme.

Included in "Other creditors" is £2,000,000 of funds provided by East Hill University Spinouts funds. The intention by East Hill is that these funds will be converted into share capital.

8. SHARE CAPITAL	<u>2006</u>	<u>2005</u>
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Authorised

65,637,504 Ordinary shares of 0.01p each	<u>£ 6,564</u>	<u>£ 6,577</u>
26,932,496 B Ordinary shares of 0.01p each	<u>£ 2,693</u>	<u>£ 2,680</u>

Issued and fully paid

	<u>Number</u>		<u>Number</u>	
Ordinary shares of 0.01p each	<u>39,169,409</u>	<u>£ 3,917</u>	<u>39,169,409</u>	<u>£ 3,917</u>
B Ordinary shares of 0.01p each	<u>26,932,496</u>	<u>£ 2,693</u>	<u>19,432,496</u>	<u>£ 1,943</u>

During the year an additional 7,500,000 B Ordinary shares were issued at a premium of 19.99p above par (2005:34,300).

PROLYSIS LIMITED**NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED
31 DECEMBER 2006**

8. SHARE CAPITAL (CONTINUED)

The company has granted the following options under its Employee Share Option Scheme:

Year of Grant	No. of 0.01p shares granted	Exercise price
2006	468,333	20p
2005	542,200	5p
2004	235,000	7p

The options are exercisable between April 2003 and December 2014.

9. MOVEMENTS IN RESERVES

	Share Capital	Share Premium	Capital Redemption	Profit and Loss
At 1 January 2006	5,860	10,097,307	1,000,161	(10,888,045)
Loss for the financial period	-	-	-	(2,352,635)
Issue of shares	750	1,490,528	-	-
At 31 December 2006	<u>£ 6,610</u>	<u>£11,587,835</u>	<u>£1,000,161</u>	<u>£(13,240,680)</u>

10. OTHER FINANCIAL COMMITMENTS

At 31 December 2006, the company had annual commitments under non-cancellable operating leases as set out below:

	<u>2006</u>	<u>2005</u>
Operating leases, which expire: within two to five years	<u>£ 75,500</u>	<u>£ 75,500</u>

11. CONTROL AND RELATED PARTY TRANSACTIONS

The company is not under the control of any individual or company.

PROLYSIS LIMITED**NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED
31 DECEMBER 2006**

12. DEFERRED TAXATION

At 31 December 2006 the company had a net unprovided deferred tax asset of £2,528,261 (2005: £2,527,403). The net deferred tax asset at 31 December 2006 is composed of a deferred tax asset of £2,470,548 arising from trading losses carried forward and a deferred tax asset of £57,713 in respect of accelerated depreciation.

No provision for the net deferred tax asset has been made at 31 December 2006 on the grounds of uncertainty over its recoverability in light of the nascent revenue streams and commitment to continued investment in research and development.